

No. 82-1066

Office-Supreme Court, U.S.
FILED

MAR 29 1983

ALEXANDER L. STEVAS,
CLERK

IN THE
Supreme Court of the United States

OCTOBER TERM, 1982

UNITED STATES OF AMERICA, *Appellant*,

v.

HARRY PTASYSKI, *et al.*, *Appellees*.

**BRIEF AMICUS CURIAE OF
THE STATE OF ALASKA**

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This brief is in support of the United States. Under Supreme Court Rule 36.4, written consent of the parties is not required.

INTEREST OF THE STATE OF ALASKA

This suit concerns the constitutionality of the "Alaskan exemption" to the Windfall Profit Tax (WPT)¹ under the Uniformity Clause of the United States Constitution.² The areas exempted by the challenged provision include portions of the State of Alaska and offshore properties adjacent to the State which are under the jurisdiction of the United States.

Alaska's interest is threefold. First, the state has a strong interest in assuring that development in the ex-

¹ Crude Oil Windfall Profit Tax Act of 1980, Article I, 26 U.S.C. (Supp. V) § 4986-4998.

² Art. I, § 8, cl. 1.

empt areas is not discouraged. In view of falling oil prices, oil properties in Alaska which were promising a few months ago are becoming marginal. If these areas are subjected to the WPT, even at a low rate, development of new reserves may not be economically feasible. The state thus stands to lose potentially substantial severance tax and royalty revenues if these areas are not developed; the nation as a whole is harmed by a disincentive to develop significant domestic reserves.

Second, to the extent that oil is produced within exempt areas in the state, that production will be more profitable without the tax. Since the WPT is a deduction against state corporate income tax, state revenues under that tax could be diminished if the areas were not exempt.³

Finally, the state, as a sovereign member of the United States, has an interest in the proper interpretation of the Uniformity Clause. The clause presents a tension between the wide latitude afforded Congress in picking and choosing appropriate subjects of taxation and a protection to the states against discrimination or favoritism. The construction given the clause by this court may have long term ramifications in resolving that tension.

SUMMARY OF ARGUMENT

The Uniformity Clause does not present an absolute bar against legislation based on geographical features. Uniformity is met if a tax "operates with the same force and effect in every place where the subject of it is found." The *Head Money Cases*, 112 U.S. 580, 594 (1884). If

³ Imposition of the tax has no effect on state severance tax or royalties from state leases.

geographical features serve to distinguish one subject from another, then Congress may describe the operation of a tax along geographical lines. The tax at issue in the *Head Money Cases* operated only in ports, and not in interior locations. But ports are necessarily located exclusively on the seacoast, which is as much a geographical feature as the geographical boundaries of the Alaskan exemption.

If a separate subject occurs only in one geographical area, then Congress, by taxing or exempting that subject, is doing so "in every place in which the subject . . . is found." *Id.* Congress is not constrained by the Clause from using geographic terms to define that subject. It would be elevating form over substance to require Congress to refrain from using geographic terms if those terms are the simplest way to describe the subject.

The question presented is whether Congress, in adopting the exemption, was defining a separate category of oil production which it chose to exempt, or whether production within the exemption is the same "subject" as other oil production and therefore, since it occurs in other locations, must be taxed with the other production. If it is a separate subject, then the exemption is valid even though it uses geographic terms in its description.

The Uniformity Clause, like the Port Preference Clause, prohibits discrimination or favoritism between the states. The Uniformity Clause speaks to political, not physical, geography. While Congress has broad leeway in picking the subjects of taxation, the Uniformity Clause limits that power by prohibiting Congress from taking the political boundaries of the states into consideration when it defines a subject of taxation. Under the Uniformity Clause, the borders of the states must be irrelevant. The Windfall Profit Tax is blind to state borders. It does

not operate, as the District Court apparently thought that it did, to relieve "one state, Alaska" from the imposition of the tax. J.S. App. A, 7a. A producer is not exempt because he produces within Alaska; tier 1 oil is taxed identically in Alaska and California. A producer is exempt if he operates in areas where there is harsh climate, lack of transportation, and high costs — considerations which have nothing to do with the political boundaries of the state.

The factors which led to the Alaskan exemption are unique to the areas defined in that exemption. For example, permafrost exists in almost the entire exempt area, and is found in no other state in the nation. The existence of permafrost has a profound affect on oil development activities. It makes the terrain extremely fragile, so that activities must be limited to the winter months to prevent damage to the ground cover. Extraordinary steps must be taken, both to protect the environment and to prevent failure of facilities.

These facilities must be built in areas that are sometimes hundreds of miles from the nearest existing ground transportation. Roadless areas of the magnitude of those found in the Alaskan exemption do not occur anywhere else in the nation.

Activities are limited, by permafrost, to the winter months when cold temperatures prevail. These are also the months of darkness. At Point Barrow in the winter, the sun does not come up for nine weeks. There is no day, anywhere else in the United States, when the sun does not breach the horizon.

Congress gave preferred or exempt treatment to many categories of oil under the WPT in recognition of the fact that some oil is relatively more expensive to develop and

produce than other oil. The Alaskan exemption is a legitimate exercise of Congressional power to recognize that these conditions of harsh climate, lack of transportation and high costs, would, if combined with the WPT, "discourage exploration and development of reservoirs . . ." in the areas within the exemption. H.R. Conf. Rep. No. 96-817, 96th Cong., 2d Sess. 103 (1980).

ARGUMENT

I The Windfall Profit Tax As It Applies In The State

Significant oil development and production in Alaska began with discovery in the Swanson River field in 1957. Production in this area, on federal leases on the Kenai Peninsula, began in the early 1960s. Offshore production in state waters in Cook Inlet followed in the late 1960s. North Slope discoveries came in the late 1960s with the Kuparuk River field in 1967 and the Sadlerochit Reservoir at Prudhoe Bay in 1968. Production from the Sadlerochit Reservoir began with the completion of the Trans-Alaska Pipeline System (TAPS) in 1978. Production from the Kuparuk field began in 1981. To date, there is no production in offshore areas adjacent to the state which are under federal jurisdiction.

Alaska presently produces approximately 1,703,000 barrels of oil per day, or about one-fifth of the total national domestic production of 8,450,000 barrels per day. Of these Alaskan barrels, approximately 1,530,000 are from the Sadlerochit Reservoir, 100,000 from Kuparuk, 65,000 from Cook Inlet and 8,000 from the Swanson River field.

Two of the many exemptions in the WPT currently apply in Alaska. First, like all state royalty interests, the state's 12.5 percent royalty from state leases is exempt as

oil from a "qualified governmental interest."⁴ Second, and the subject of this appeal, oil from the geographic area described in Section 4994(e) is "exempt Alaskan oil."⁵ That section provides:

For purposes of this chapter, the term 'exempt Alaskan oil' means any crude oil (other than Sadlerochit oil) which is produced—

- (1) from a reservoir from which oil has been produced in commercial quantities through a well located north of the Arctic Circle, or
- (2) from a well located on the northerly side of the divide of the Alaska-Aleutian Range and at least 75 miles from the nearest point on the Trans-Alaska Pipeline System.

Production in Prudhoe Bay (Sadlerochit), Cook Inlet and Kuparuk is all on state leases under a royalty of 12.5 percent. The "Alaskan exemption" includes oil produced north of the Arctic Circle (except Sadlerochit) or north of the Alaska-Aleutian Range divide and more than 75 miles from TAPS. Cook Inlet is south of that divide, and therefore not exempt. Swanson River is similarly south of the divide and not exempt. Prudhoe Bay production from the Sadlerochit reservoir (all North Slope production except Kuparuk) is specifically not exempt. Thus, the only oil exempt from the WPT under the "Alaskan exemption" is the non-royalty portion of Kuparuk production:

⁴ Section 4991(b)(1).

⁵ Section 4991(b)(3).

Alaskan Oil Production Under the WPT

Barrels Per Day

Field:	<u>Sadlerochit</u>	<u>Kuparuk</u>	<u>Cook Inlet</u>	<u>Swanson</u>	<u>Total</u>	<u>% of Total</u>
Production	1,530,000	100,000	65,000	8,000	1,703,000	100%
State Royalty (exempt)	191,250	12,500	8,125	0	(211,875)	12.4%
Alaska Exemption	0	87,500	0	0	(87,500)	5.1%
Total Barrels Per Day Subject to Tax:					1,403,625	82.6%

Thus, 5 percent of Alaska production is exempt under the Alaskan exemption. More than 82 percent of Alaskan production is taxed.

The WPT sets varying rates of taxation for various categories of oil. Thus, independent producer oil, stripper oil, front-end and incremental tertiary oil, and heavy oil are all treated with some favor or exempt altogether. None of these provisions applies to Alaskan oil to any significant degree; Alaska has no stripper wells, no tertiary recovery projects, no heavy oil and very little oil produced by independent producers. Thus, Alaskan oil which is taxed is taxed at the highest rate.

II The Uniformity Clause Does Not Prohibit Congress From Describing An Appropriate Subject For Taxation Or Exemption In Geographic Terms

Congress has wide latitude in picking and choosing among appropriate subjects of taxation.⁶ This power extends to making distinctions among similar subjects. In interpreting the Uniformity Clause,⁷ this Court noted that tariff acts "frequently contained an elaborate system of minimum classifications and compound duties as well as exemptions for importations below a certain level." *Knowlton v. Moore*, 178 U.S. 41, 93 (1900). This broad power is limited by the requirement imposed by the Uniformity Clause. That requirement is met when a tax "operates with the same force and effect in every place

⁶ *Fernandez v. Wiener*, 326 U.S. 340, 352 (1945) ("Congress has a wide latitude in selection of objects of taxation."); *Sonzinsky v. United States*, 300 U.S. 506, 512 (1937) ("Congress may select the subjects of taxation, choosing some and omitting others.").

⁷ "The Congress shall have the power to lay and collect taxes, duties, imposts and excises, . . . ; but all duties, imposts, and excises shall be uniform throughout the United States."

where the subject of it is found." *The Head Money Cases*, 112 U.S. 580, 594 (1884).

The District Court held flatly that "[d]istinctions based on geography are simply not allowed." J.S. App. A, 7a. But this Court's prior cases indicate that this per se rule is untenable. In the *Head Money Cases*, the tax at issue was levied on passengers from foreign ports arriving by steam or sail, but not on passengers arriving from foreign countries by inland transportation. The Court found that the tax applied uniformly in all ports and declined to invalidate it because it did not apply in the interior. 112 U.S. at 594. But ports necessarily are found only on the seacoast, which is as much a geographical feature as the Alaska-Aleutian Range or the Arctic Circle. It would be elevating form over substance to conclude that the valid tax at issue in the *Head Money Cases* would become unconstitutional if the tax were written to apply only within a certain number of miles of the sea. This is precisely what this court has said in ruling on related constitutional provisions.

In interpreting the uniformity provision of the Bankruptcy Clause,⁸ this Court stated that the provision "does not deny Congress power to take into account differences that exist between different parts of the country, and to fashion legislation to resolve geographically isolated problems." *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 159 (1974). The Rail Act was written to apply only in a limited geographical region. In concluding that the regional act did not violate the Bankruptcy Clause uniformity provision, the Court relied on the analysis of the *Head Money Cases* and stated that its "construction

⁸ Art. I, § 8, cl. 4.

of the Bankruptcy Clause's uniformity provision comports with this Court's construction of other 'uniform' provisions of the Constitution." Id. at 160.

The Court quoted the holding of the *Head Money Cases* that "the evil to be remedied by this legislation has no existence on our inland borders, and immigration in that quarter needed no such regulation" and held that "[s]imilarly, the Rail Act is designed to solve the evil to be remedied, and thus satisfies the uniformity requirement of the Bankruptcy Clause." Id. at 161. The Court refused to distinguish the Rail Act from the head tax statute on the grounds that the former "by its own terms . . . applies only to one designated region," and stated that the argument was "without merit." Id. Consequently, the conclusion can be drawn that it is legitimate for Congress to take geographic differences into account without running counter to the Uniformity Clause so long as the evil to be remedied differs along geographic lines. The Congressional debates and reports show that Congress was intent upon remedying the peculiar evil presented by harsh climate, lack of transportation facilities, and high costs associated with production when it adopted the Alaskan exemption. These considerations are addressed at Section IV of this brief.

A second line of analysis leads to the same conclusion. In the *Head Money Cases*, the Court could have viewed the statute as taxing the "subject" of the importation of passengers from foreign countries. As such, the tax might not have been uniform if it did not apply in the interior. Instead, it noted that the tax was "an excise duty on the business of bringing passengers from foreign countries into this *by ocean navigation*" and easily found that the subject of taxation was taxed uniformly wherever it was found. 112 U.S. at 594, emphasis added.

It is clear from the face of the WPT that the Act does not simply tax the single subject of oil production, or even the single subject of a windfall profit (defined as removal price less adjusted base price). The Act taxes a wide variety of related subjects, including what Congress perceived as the windfall attributable to independent producer oil, stripper oil, tertiary oil, heavy oil, and Indian oil. Congress has the power to make such distinctions among related subjects, tax some at a heavy rate, some at a lower rate, and exempt others altogether.

Thus, the question becomes whether Congress, in adopting the Alaskan exemption, was defining a separate and distinct category of oil production which it chose to exempt, or whether production within the Alaskan exemption is the same "subject" as some other oil production which since it occurs in other locations, must be taxed at the same rate.⁹ Clearly, if it is a separate "subject," the exemption does not offend uniformity; as the Court in the *Head Money Cases* pointed out, "[i]s the tax on tobacco void, because in many States no tobacco is raised or manufactured?" 112 U.S. at 594. As will be discussed more thoroughly later, there is ample evidence that oil produced within the geographic limits of the Alaskan exemption is properly treated as a separate subject from other new oil, just as oil of an independent producer is treated separately from oil of an integrated producer, or stripper oil from tertiary oil.

⁹ "[W]hatever plan or method Congress adopts for laying the tax in question, the same plan and the same method must be made operative throughout the United States; that is to say, that wherever a subject is taxed anywhere, the same must be taxed everywhere throughout the United States, and at the same rate." *Knowlton v. Moore*, supra, 178 U.S. at 84.

The Uniformity Clause speaks to political, not physical geography; that is, the borders between the states. So long as Congress is exercising its nearly unlimited power to pick and choose among subjects of taxation, an act should not fail for want of uniformity even though a subject is defined in geographic terms. If, however, Congress discriminates among the states by exposing some to a higher rate of taxation or exempting others, and that discrimination is based on the political boundaries of the states, then the Uniformity Clause is violated.¹⁰

III The Alaskan Exemption Does Not Violate The Uniformity Clause Because It Does Not Prefer Or Discriminate Among The States

The uniformity required by the Uniformity Clause is geographical rather than intrinsic. *Knowlton v. Moore*, *supra*, 178 U.S. at 106. However, this Court has never been asked to decide precisely what is meant by that geographical uniformity. The language of prior decisions, including those on related constitutional provisions, indicates that the geography referred to is political geography rather than geography based on physical features. That is, the Uniformity Clause prohibits discrimination or favoritism between states, made for or against the states on the basis of the political boundaries of those states.

Congress has unfettered discretion in choosing among the subjects of taxation and has the power to make distinctions based on whatever differences between related

¹⁰ Taxpayer and association appellees have argued that if the Alaskan exemption is upheld because it is supported by a rational basis, then the Uniformity Clause becomes "merely" an Equal Protection Clause. Appellees' Motion to Affirm at 9. But it is the added protection of freedom from political favoritism or discrimination among the states that gives the Uniformity Clause its separate validity.

subjects it perceives as important. The Uniformity Clause makes one limitation on that power. Under the Clause, Congress may not use distinctions among or between the states, as political entities, as a basis for distinguishing among subjects of taxation. For example, if alcohol is taxed at ten cents on the gallon in Illinois, it may not be taxed at a nickel in Wisconsin solely because it is found within the borders of Wisconsin.¹¹

The Uniformity Clause "look[s] to the forbidding of discrimination as between the states." *Knowlton v. Moore*, 178 U.S. at 89. The Court in that case concluded that "the possible discrimination against one or more states was the only thing intended to be provided for by the rule which uniformity imposed upon the power to levy duties, imposts and excises . . ." *Id.* The political boundaries of the states must be irrelevant when Congress levies the listed taxes so that, for federal purposes, it does not matter on which side of a state's border an activity or subject of taxation occurs. Thus, a tax which is blind to state political borders should be valid notwithstanding that a portion of its operation speaks to unique regional circumstances.

This construction is supported by this Court's explanation of the related Port Preference Clause.¹² This Court has held that the Uniformity Clause and the Port Preference Clause were "one in purpose, one in their adoption."

¹¹ Oil production is peculiarly amenable to a distinction based on physical geography, since the occurrence of oil and, therefore, the conditions under which it is produced, is entirely a function of physical geography. Thus, it would be difficult to imagine a justification for, for example, a tax distinction between alcohol on one side or the other of the Mississippi; oil, however, must be produced where it is found.

¹² Art. I, § 9, cl. 6.

Knowlton v. Moore, 178 U.S. at 105.¹³ In *Pennsylvania v. The Wheeling and Belmont Bridge Co.*, 59 U.S. (18 How.) 421 (1855), it is argued that Congressional legislation authorizing a bridge across the Ohio River at Wheeling, Virginia was void since the bridge obstructed navigation to Pittsburgh, and thus preferred the port of Wheeling over Pittsburgh. The Court held that the Clause "looks to a prohibition against granting privileges or immunities to vessels entering or clearing from the ports of [one] state over those of another," and that "it is a mistake to assume that Congress is forbidden to give a preference to a port in one state over a port in another." This Court explained:

The truth seems to be, that what is forbidden is, not discrimination between individual ports within the same or different states, but discrimination between states; and if so, in order to bring this case within the prohibition, it is necessary to show, not merely discrimination between Pittsburgh and Wheeling, but discrimination between the ports of Virginia and those of Pennsylvania.

Id. at 435.

Under this analysis, it would be necessary to show that the WPT discriminates between states; that is, that Alaska, as a political entity, is preferred. The Wyoming District Court apparently concluded that such a preference was written into the Act. "The Act, on its face, says that one state, Alaska, is not subject to the same tax, at the same rate as all other states." J.S. App. A, 7a. An Act which exempted Alaska *qua* Alaska would indeed give rise to scrutiny under the Uniformity Clause. But the WPT does not work that way.

¹³ A comprehensive discussion of the relationship between the Uniformity Clause and the Port Preference clause appears at pp. 23-27 of appellant's brief.

An oil producer is not relieved of obligations under the WPT because he enters the state of Alaska. New oil in Cook Inlet is taxed at the same rate as new oil in Long Beach. Tier 1 oil at Prudhoe Bay is subject to the same tax, and at the same rate, as tier 1 oil elsewhere. Certain producers are exempt on certain properties where conditions of harsh climate, lack of transportation and high costs prevail. But offshore production north of Prudhoe Bay will be exempt ¹⁴ if it is within the political borders of Alaska, and it will be exempt if it is outside the borders of the state, in federal waters more than three miles from land. The exemption is blind to political borders.¹⁴

Thus, oil production is exempted not because it is Alaskan, but rather because it takes place under unique circumstances which are a function of physical geography. The exemption is based on the physical geography of the mountain range, the Arctic Circle, and the pipeline corridor, and extends "throughout the United States" to the limit of the nation's taxing jurisdiction.¹⁵ The exemption is not the sort of distinction that the Uniformity Clause prohibits.

IV The Alaskan Exemption Describes A Separate Category Of Oil Production Which Is Legitimately Exempt From The Windfall Profit Tax

The Congressional debates and reports amply indicate that several concerns led to the Alaskan exemption: harsh

¹⁴ The fact that only 5 percent of present Alaskan production is exempt from the WPT (Section I, *supra*) is evidence that the exemption does not prefer Alaska over other states.

¹⁵ It is an accident of political history that the United States has but one state in the arctic-subarctic regions. If Alaska were split into several states, or if by treaty with Canada the Yukon became a state, the exemption would operate throughout parts of those states without reference to the borders between them.

climate, fragile environment, the transportation implications of remote location, and high costs. As Senator Stevens stated:

Development and production of [Alaskan] reserves . . . is by all accounts expensive and difficult. Short construction seasons and the effects of severe arctic winters take their toll on men and equipment. Special steps must be taken to preserve a fragile arctic environment. The costs of transportation and labor are high.

125 Cong. Rec. S17422 (daily ed. Nov. 28, 1979). Senator Gravel noted that exploration and development in frontier areas were subject to a greater degree of risk:

Major factors contributing to these increased risks are severe weather conditions, remoteness, sensitive environmental and geological characteristics, and a lack of normal social and industrial infrastructure.

125 Cong. Rec. S16327 (daily ed. Nov. 8, 1979).

As a result of these factors, the conference report indicated that the exemption "reflects the concern of the conferees that taxation of this production would discourage exploration and development of reserves in areas of extreme climatic conditions," H.R. Conf. Rep. No. 96-817, 96th Cong., 2d Sess. 103 (1980). The many and various references to these concerns have been set out by appellant and other amici, and will not be repeated here. Each deals with the concerns expressed by Alaska's Senators, and the conclusion that if oil in the exempt area were taxed, the development of significant national reserves might be discouraged.

Congress recognized that these factors could be anticipated to have an effect on the feasibility of future production in Alaska. The question is whether Congress could have concluded that oil production in the exempt area was

a separate subject from oil production anywhere else in the United States so that it could be given different tax treatment; whether harsh climate, lack of transportation and high costs presented a peculiar evil which Congress was addressing by the exemption.

THE AREA

The area described by the Alaskan exemption includes most of the state in terms of acreage. The Alaska-Aleutian Range sweeps up from the Aleutians in the southwest, and describes an arc which reaches its northermost extension at Denali (Mt. McKinley) and the three peaks of Deborah, Hess and Hayes, approximately 75 miles south of Fairbanks. See map, Appendix A. It then turns toward the southeast again as it crosses the Canadian border. The pipeline corridor described in the exemption reduces the exempt area by a 150 mile wide swath going north from the range across Fairbanks, past the Yukon River to the Arctic Circle, about 100 miles north of Fairbanks.

But acreage is probably the only measurable indicator of size that puts the majority of the state in the exempt area. Substantially all of the state that is developed is outside the exemption. Many a visitor to Alaska is likely to return home satisfied that he or she has seen most of the state having never set foot in the exempt area. Many Alaskans have never been there. Anchorage, Fairbanks and Juneau are not exempt. Kodiak Island, the Kenai Moose Range, the Inland Passage, Glacier Bay, Seward, Cordova, Homer, Yakutat, Wrangell and Ketchikan are all south of the line drawn by the exemption. McKinley Park, which straddles the divide, is partially within the exemption. Nome, Kotzebue, Barrow and Bethel are the only "major" settlements in the exempt area; Bethel, the largest, has a population of approximately 3550. More

than 85 percent of Alaska's population resides south of the exemption.¹⁶ None of Alaska's farmland, either in the Matanuska-Susitna valley or the Delta area, is in the exempt area. Chances are quite good that if one landed at an airport with a control tower, that airport was south of the exemption. Of the three major highways—the Richardson, Glenn and Parks, the first two are entirely outside the exemption; the Parks, which connects Anchorage and Fairbanks, is more than 75 miles from TAPS for a short stretch from the divide north to about the northern border of McKinley Park. Most of the economic activity in the state is outside the exemption, with the major exception being the Bristol Bay fishery. And, as was explained at Section I *supra*, almost all Alaska's oil is produced outside the exemption.

It cannot be questioned that Alaska has a harsh climate, a fragile environment, a general lack of transportation facilities and resultant high costs. But in order to understand the effect that Congress perceived the combination of these factors might have been on future oil production, a little more is necessary than the bare assertion that these conditions exist.

¹⁶ Alaska Planning Information, Alaska Department of Labor, January, 1983, Table II-3, Population by 1980 Census Areas. This figure is approximate since census areas do not follow the line of the Alaskan exemption. Thus, Bristol Bay was treated as exempt even though a small portion of its population would be outside the exemption, and Fairbanks-North Star Borough was treated as non-exempt although a few residents would be more than 75 miles from TAPS. If the North Slope Borough, which includes many Prudhoe Bay workers, and the Aleutians are considered entirely exempt, 86.4 percent of Alaskans live outside the exempt area. If those two census areas are ignored, then 89.8 percent are outside the exemption.

COSTS

Climatic, environmental and transportation difficulties do not, in any intrinsic sense, justify an exemption from a tax on profit; if a profit is made under those conditions, and profits are taxed, then production from these areas should arguably be taxed. But the word "profit" in the "Windfall Profit Tax" makes the title of the Act a misnomer. The Act does not tax "profit," that is, gross income less expenses. It is an excise tax on certain statutorily identified income, a tax that is levied without regard to the costs associated with earning that income.¹⁷ If two barrels of oil fall within the same category of the WPT, they are taxed at the same rate regardless of relative profitability.¹⁸ Within each taxing category, the WPT is blind to profits.

But the WPT does not tax all windfall profits at the same rate. The Act sets up an intricate scheme whereby oil is taxed differently on the basis of a wide variety of differences: independent producer or integrated producer; stripper oil; front end or incremental oil from a tertiary recovery project; heavy oil; or new oil. Many of these differences reflect a Congressional recognition that costs are not identical in every type of production. Since an overriding purpose of the WPT was to insure that production was not discouraged, Congress concluded that

¹⁷ Senator Stevens stated: "This is an excise tax. It has nothing to do with costs." 125 Cong. Rec. S17478 (daily ed. Nov. 29, 1979).

¹⁸ Two barrels produced by integrated producers in Tier 1 might have an identical windfall profit of, for example, \$3.00. But the first might have a profit below the base price of \$5.00 while the second, due to higher costs, might have a profit below the base price of only \$1.00. Thus, both would pay the same tax of 70 percent on the three dollars, or \$2.10, but that amount would be 52.5 percent of total profit for the first producer and only 26.25 percent of profit for the second.

recognition of the varying costs related to development and production of oil was necessary to accomplish the purposes of the Act.

Transportation and climatic conditions add substantially to the cost of developing and producing oil in Arctic and sub-Arctic Alaska. It is not possible for the state to present a cumulative, quantitative estimate of comparative costs here and elsewhere, since oil producers consider the information proprietary. But some costs can be estimated, and at least a part of the overall picture can be seen.

The American Petroleum Institute reported comparative costs for drilling wells in Alaska, California, Louisiana and Texas in 1976. For onshore wells, the average cost in Alaska was \$3,181,000 compared to the next highest cost in Louisiana of \$292,000. The cost per foot was higher, and the average depth was higher. For offshore wells (primarily Cook Inlet at that time) the cost per foot was close to other parts of the nation, but the average depth was much greater. Average cost in Alaska was \$2,046,000 compared with the next highest cost of \$1,617,000 in Texas.¹⁹

Standard & Poor's Industry Surveys reported the cost per foot to drill and equip wells in 1980 in various regions by depth intervals. Looking at a sampling of depth intervals in the four states in the previous report, from 2,500 feet to 3,749 feet, Alaskan cost per foot was \$898 compared with \$93 in California, \$36 in Louisiana, and \$40 in Texas. In the 7,500 to 9,999 interval, Alaska was \$305, California \$91, Louisiana \$135 and Texas \$70. At 15,000

¹⁹ 1976 Joint Association Survey on Drilling Costs, API, December 1977.

to 17,499 feet, Alaska was \$1,058 with the next runner up, Louisiana, at \$293.²⁰

Senator Gravel presented figures showing that "[t]he cost of drilling a well in Alaska is 15 times greater than the cost of drilling a well in the rest of the United States." 126 Cong. Rec. S2630 (daily ed. Mar. 19, 1980).

The cost of wells is only a fraction of total development costs. The climatic and transportation factors discussed below affect every phase of activity. Workers and equipment must be transported great distances. Workers are paid extremely high wages,²¹ and must be fed and housed on site. If, for example, operations are suspended at a drilling site due to spring thaw, an experienced crew might be kept standing by for as long as two weeks. But it can cost \$50,000 to \$60,000 per day to keep a crew on stand-by. The factors influencing these costs are unique to a portion of Alaska.

CLIMATE

Visitors to Alaska are often surprised to discover that it can be quite hot in Fairbanks on a July afternoon. The long summer days, with the sun scarcely dipping below the horizon and twilight merging into dawn, belie the effect that winter has on the environment. But in the interior and in the north, summer is a brief notorious period of teeming life and growth, preceded by a few days of spring and followed by a few days of fall. Winter takes the rest.

²⁰ Standard & Poor's Industry Surveys, Oil-Gas Drilling and Services, Vol. 150, No. 40, Sec. 1 (Oct. 7, 1982) 0118.

²¹ Senator Gravel stated that a "lower 48 worker costs approximately \$9 per hour while the same worker on the North Slope costs approximately \$41 per hour." *Id.*

That the winters are cold cannot be contested. But it is also cold in Minnesota, in North Dakota and in Idaho. Once in a while, it is even unexpectedly warm in Alaska; every year or so the national media delights in reporting that it is colder in Miami on a December day than in some Alaskan city. But the overall, long term, average temperature is colder in Alaska than in any other part of the nation. The obvious physical manifestation of this cold is the existence of permafrost, a common occurrence in Alaska which simply does not exist in other states (except perhaps at extreme altitudes).

Permafrost is generally defined as ground which has remained frozen from one winter through the next,²² although some authors use two years.²³ Of all the environmental and climatic conditions which make development more difficult in the north than in other parts of the nation, permafrost is probably the most critical. Permafrost makes engineering difficult, and makes the terrain fragile.

The line of discontinuous permafrost in Alaska is remarkably close to the line drawn by the Alaskan exemption. See Appendix A. This line continues through the Yukon Territory, along the northern portion of the Canadian Provinces, and meets the Atlantic Ocean in Newfoundland. It does not enter the contiguous United States.²⁴ Permafrost varies from a few inches thick in the

²² Alaska Regional Profiles, Yukon Region, University of Alaska (prepared for the State of Alaska and The Joint Federal-State Land Use Planning Commission for Alaska) 98.

²³ Environmental Atlas of Alaska, University of Alaska (1969).

²⁴ Permafrost, North American Contribution, Second International Conference, National Academy of Sciences (1973) 73 (Brown and Pewe, Distribution of Permafrost in North America).

southern areas of its occurrence to 2,000 feet thick at Prudhoe Bay. It also varies in its composition, from bedrock to fine, silty soil. But the general rule is that permafrost of whatever description must be left undisturbed.

Most of the permafrost area in the state supports some surface vegetation, whether forest or tundra or the mosses and sedges of the North Slope. But permafrost is not conducive to plant growth. It keeps the root zone cold, and "prevents the penetration of roots, resulting in a shallow, lateral root system. Permafrost prevents water percolation, so the active layer is boggy, poorly aerated, and improperly nourished."²⁵ This fragile vegetation insulates the permafrost; if disturbed, thawing and damage occurs. "Little alteration of the permafrost may occur through removal of trees or brush, but severe damage occurs when the moss or peat cover is disturbed. Vehicle traffic across tundra areas is a major cause of this type of disturbance. The resulting permafrost thaw and subsidence often leads to local flooding, drainage diversion and soil erosion."²⁶

Because of the necessity to protect the surface vegetation from disturbance, vehicles and machinery can be used only during the winter months when the surface is frozen and covered with snow. The Alaska Department of Natural Resources issues land use permits for seismic operations, and places restrictions in oil leases. These authorizations contain standard restrictions which effectively limit those operations to the period between freeze-up and break-up, except on existing roads and

²⁵ Alaska Regional Profiles, *supra*, at 100.

²⁶ *Id.*

facilities.²⁷ Once a road or other facility is built it may be used year round.

Permafrost additionally imposes restraints on construction which are absent in other parts of the world. Just as disturbance of the protective vegetative mat will lead to thaw, erosion and environmental degradation, so will construction on permafrost lead to subsidence, icing, slumping and frost heaves, if proper steps are not taken to insulate the frozen soil. "Thawing of permafrost and cycles of freezing and thawing in the active layer damage highways, railroads, airstrips and other facilities."²⁸ Extensive on-site reconnaissance must be conducted before any construction project, without which "considerable risk of construction failure at worst and delayed construction schedules at best are inevitable."²⁹

Once the extent and nature of the conditions are known, special consideration techniques must be used which may include thick gravel pads, elevation of pipelines and buildings on supports and pilings, the use of refrigerated pilings, and specially designed bridges. The

²⁷ Typical restrictions are: "The use of ground contact vehicles for off-road travel must be limited to those areas which have adequate ground frost and snow cover to prevent damage to the ground surface." "After 15 April, the use of ground contact vehicles in wetlands and other areas of weak soil conditions (e.g., North Slope tundra) will be subject to termination within seventy-two (72) hours . . ." "Support vehicles must be operated in a manner such that the vegetative mat of tundra is not disturbed. Blading or removal of tundra is strictly prohibited, except as approved by the Director . . . Filling of low spots and smoothing by the use of snow and ice is allowed." Alaska Department of Natural Resources, *Seismic Stipulations*, Revised: November 1982. Leases contain similar restrictions.

²⁸ Alaska Regional Profiles, *supra*, at 103.

²⁹ *Id.*

engineering problems and unique solutions for the construction of TAPS are well known. But the best design is sometimes not good enough: "Alyeska Pipeline Service Company has begun a major modification of its buried pipeline crossing in the Dietrich River main channel. As a result of thawing in an undetected ice lens deep beneath the river bottom, settlement of the line has been severe enough to require repairs . . ."³⁰

The restriction of construction and seismic activities to the winter months because of permafrost reduces the time available for exploration and development activities in permafrost regions to less than half the time available in other parts of the nation. Further, the time to which activity is restricted is the time of harshest climate. Temperatures in Alaska's interior commonly reach -40 to -50 degrees Fahrenheit; a low of -80 degrees Fahrenheit was recorded in 1971.³¹ Cold temperatures are compounded by wind chill, particularly in coastal regions. It is difficult to quantify the effects of these climatic conditions on men and equipment working in them. A few examples will serve as illustration.

Vehicles, including cars, trucks, airplanes, all-terrain vehicles, tractors and cranes, must be prepared for and nursed through the cold. Keeping a car running through a Fairbanks winter can seem like a full-time job. After the common precautions of antifreeze and light oil are taken, many other steps are often necessary. A vehicle must be preheated in some manner before it will start—even light oil is nearly solid at -40 degrees Fahrenheit. Similarly, the battery must be warmed, as a battery at that temper-

³⁰ Alaska Report, Petroleum Information Corp., Vol. 29, No. 8 (2-23-1983) at 2-3.

³¹ Alaska Regional Profiles, *supra* at 15.

ature is next to useless. Tires inflated properly for operating temperatures deflate when cooled and freeze square on the bottom, creating a bumpy ride which jars both car and driver. Pliant seals which keep liquids in their proper places freeze and split, spilling liquids. Emergency brakes cannot be used, as the cable will lock and snap. Once started, a vehicle cannot be shut down for long away from home port or it will not restart.

Heavy protective clothing makes the simplest job clumsy and cumbersome. Uninsulated flesh cannot come into contact with metal or it won't come loose again, so valves and other moving parts must be designed so that they can be operated with thick mittens, or cumbersome tools must be used to work them. Overexertion results in frozen lungs from sucking in cold air or in perspiration which can freeze and endanger life. Protective goggles fog up and freeze to the face.

Teams of seismic crews moving over the winter terrain frequently become isolated from air support due to ice fog (as rivers freeze down, running water becomes compressed and breaks through the surface, evaporating quickly into dense frozen mist) or blizzards or blowing ground snow. Sometimes it is just too cold to fly.

The winter is also the time of darkness. The Arctic Circle is the latitude at which the sun does not breach the horizon on winter solstice. The higher the latitude, the darker the winter days. At Point Barrow, the sun does not come up at all from November 15 until January 25. Fairbanks has 3½ hours of sun on winter solstice, and Anchorage has 5½.²² Since winter is the construction season, work must be done in the dark, or artificial lights

²² Environmental Atlas of Alaska, *supra*, at 53.

used. Nowhere else in the United States is so dark in the winter.

The cumulative effects of these climatic conditions on oil development and production cannot be accurately estimated; but it is undeniable that they present a peculiar difficulty absent from more temperate climates.

TRANSPORTATION

The existing surface transportation system in Alaska can be described in a few short sentences. Fairbanks is the northernmost population center, and it is slightly south, and a good deal east, of the center of the Alaskan land mass (excluding the Aleutian chain and the Southeast panhandle). The Alaska Highway comes northwest from Canada and terminates at Fairbanks. The Glenn Highway connects Anchorage with the Alaska Highway. The Parks Highway connects Anchorage and Fairbanks. These three highways, forming a triangle in the southeast quarter of the state, comprise the entire network of major highway transportation in the state. Minor highways go for short distances north from Fairbanks, south from Anchorage, and connect Valdez with the system. The TAPS haul road (not open to the public) parallels the pipeline north from Fairbanks to Prudhoe Bay. Truly bad roads can be traversed to Dawson (Canada), McCarthy and a handful of other locations. There are simply no roads west of Cook Inlet (Anchorage) or, with the exception of the haul road, north of the Yukon-Kuskokwim Rivers. Thus, the entire western and northern part of the state is accessible only by air. See map, Appendix A.

Rail transportation parallels the Parks Highway between Anchorage and Fairbanks, and continues south of Anchorage to Whittier. The Southeastern panhandle is served by a ferry system between that area and Seattle, and sea transportation is available to Anchorage. More

northern ports do not remain ice-free. This surface transportation system is outside the exempt area. See map, Appendix A.

Roadless areas in the contiguous United States are small pockets here and there in the general network of roads and highways. It is impossible to be more than 100 miles from a road in the lower 48 states. But a lack of surface transportation is the rule in the exempt portion of Alaska rather than the exception.

Lack of transportation affects not only the expense of exploration and production, but the value of the oil once it is produced. Thus, an Alaskan producer must add some \$7 or \$8 per barrel in transportation costs from the North Slope to his production costs when he competes in the market in the lower 48 states. His incentive to produce is affected by this consideration.³³

SUMMARY

The State of Alaska has presented an overview of some of the factors which Congress perceived served to distinguish oil production in certain regions in Alaska from oil production elsewhere. Congressional recognition of the risks, difficulty and expense of production in these regions resulted in exemption from the tax. This exemption reflects the legislative judgment that "taxation of this production would discourage exploration and development of reservoirs in areas of extreme climatic conditions." H.R. Conf. Rep. No. 96-817, 96th Cong., 2d Sess. 103 (1980).

³³ The WPT would reduce the removal price by this cost, but the effect of the disincentive is not eliminated by this treatment. See, Brief of Amicus Curiae Atlantic Richfield Company at footnote 27.

If severe climate, represented by the line of discontinuous permafrost, is considered in conjunction with access, within 100 miles, to existing transportation facilities, a line very close to the line drawn by the Alaska exemption emerges.³⁴ These circumstances, and others, set oil development in this region apart from similar activity anywhere else in the nation. Permafrost does not occur within the contiguous United States. There are no areas more than 100 miles from a road. The temperature does not reach -70 degrees Fahrenheit south of Canada. There are no completely dark days anywhere in the Lower 48. Within the United States, each of these factors is unique to portions of Alaska.

Each of these factors affects the nature of oil development and production activities, and is therefore a legitimate basis for a congressional distinction between oil production within the exempt area and other parts of the nation. None of these factors is based on a preference for Alaska as a political entity. Oil production in this area, thus, can properly be viewed as a separate subject from oil production elsewhere. As such, Congress may exercise its broad discretion and choose not to tax that subject. In so doing, it has exempted the subject wherever it occurs. It may, without violating the Uniformity Clause, address the peculiar "evil" presented by these factors and fashion legislation designed to cure that evil. The Alaskan exemption is constitutional.³⁵

³⁴ The transportation system in Alaska may change dramatically in the next century as the state becomes more settled. But the WPT expires of its own terms in 1993. Section 4990. Major additions to that network in that period will in all likelihood be a function of oil and gas development and financed by that industry.

³⁵ The State of Alaska takes no position on the severability of the Alaskan exemption if it is unconstitutional.

CONCLUSION

The judgment of the district court should be reversed.

Respectfully submitted,

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